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No. 84-1076

In The

Supreme Court of the United States

October Term, 1984

TRANSCONTINENTAL GAS PIPE LINE CORPORATION,

Appellant,

v.

THE STATE OIL AND GAS BOARD OF MISSISSIPPI AND COASTAL EXPLORATION, INC., et al,

Appellees.

On Appeal from the Supreme Court of Mississippi

COASTAL EXPLORATION, INC.'S MOTION TO DISMISS OR, IN THE ALTERNATIVE, TO AFFIRM THE DECISION OF THE SUPREME COURT OF MISSISSIPPI

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QUESTIONS PRESENTED

1. *The Preemption Question:* Do the Natural Gas Act of 1938 (NGA) and the Federal Energy Regulatory Commission's (FERC) jurisdiction under § 1(b) of the NGA apply to the "first sale" of gas which has been determined to be deregulated "deep, high-cost natural gas" under Section 107 of the Natural Gas Policy Act of 1978 (NGPA)?

2. *The Commerce Clause Question:* Does the requirement that an interstate gas purchaser must offer to take federally-deregulated gas ratably from the wells which produce from a gas pool and must offer to pay the non-contract owners in the pool a "market price" for their gas constitute a burden on interstate commerce?

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THIS CASE SHOULD BE DISMISSED OR AFFIRMED

This case should be dismissed or, alternatively, the decision of the Mississippi Supreme Court should be affirmed for lack of a substantial federal question because it is clear that the simple state ratable take requirement at issue does not directly or indirectly conflict with either the NGA or the NGPA, nor does the requirement constitute a burden on interstate commerce. Because Congress has so clearly and unequivocally declared that the NGA and FERC's jurisdiction under the NGA *never* apply to the first sale and purchase of the federally-deregulated gas in question, a state, once again, is free to make the simple two-fold requirement that, if and when a gas purchaser takes federally-deregulated gas from a gas pool, (1) the purchaser must offer to take whatever quantities of that gas it desires ratably from the wells which produce from the pool (in order to prevent drainage, reservoir damage and "waste", and to afford each owner in the pool the opportunity to recover his share of gas), and (2) when the gas is actually taken, the purchaser must offer to pay a market price for the gas of those owners with whom the purchaser does not have a written contract. *Transcontinental Gas Pipe Line Corp. v. State Oil & Gas Board of Mississippi*, 457 So.2d 1298, 1327, 1331 (Miss. 1984).

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SUMMARY OF THE ARGUMENT

1. *The Preemption Question:* Do the NGA and FERC's jurisdiction under Section 1(b) of the NGA apply to the "first sale" of gas which has been determined to be deregulated "deep, high-cost natural gas" under Section 107 of the Natural Gas Policy Act of 1978 (NGPA)? No. The answer to that narrow question lies in the clear language of Section 601(a)(1) of the NGPA. Some case history is in order. In *Cities Service Gas Company v. Peerless Oil & Gas Company,* 340 U.S. 179 (1950), the Court rejected constitutional challenges to a state ratable take/minimum price order entered against an interstate gas purchaser. The Court, however, did not consider the effect of the NGA on the validity of such an order. That effect was considered thirteen (13) years later in *Northern Natural Gas Co. v. State Corporation Commission of Kansas,* 372 U.S. 84 (1963), which held invalid a state ratable take order directed against an interstate pipeline company because the state's order invaded the Federal Power Commission's (FPC) *then-existing* exclusive regulatory jurisdiction under Section 1(b) of the NGA, jurisdiction and regulatory authority which, at that point in time, extended to a producer's sale and a pipeline's purchase of natural gas destined for the interstate market. That jurisdiction and that regulatory authority were eliminated by Congress in 1978 when it enacted the NGPA. Specifically, Section 601(a)(1) of the NGPA provides that the first sale of, *inter alia,* deregulated "deep, high-cost natural gas" natural gas is *never* made subject to either the NGA or FERC's jurisdiction under the NGA. Because FERC no longer has any statutory authority to regulate the first sale transaction involving that category of natural gas, the statutory reasons for the result in

Northern Natural no longer exist in the case of that category of gas, and the state, once again, is free to enforce a ratable take requirement to that first sale transaction. *Peerless, supra.*

2. *The Commerce Clause Question:* Does the requirement that a gas purchaser must offer to take federally-deregulated gas ratably from the wells which produce from a pool and must offer to pay the non-contract owners in the pool a "market price" for their gas constitute a burden on interstate commerce? No. That precise question was answered thirty-five (35) years ago in *Peerless,* which rejected the claim that a state ratable take order violates the Commerce Clause. *Northern Natural,* decided on narrow statutory grounds, noted that *Peerless* remained good law as to the constitutional challenges to a state ratable take order. *Stare decisis,* however, is not the only reason why the Commerce Clause "question" in this case is not substantial. It is undisputed that there is no actual conflict or collision between the federally-deregulated first sale and purchase transaction which the state seeks to affect, and the subsequent pipeline transportation and resale activities which FERC continues to regulate on a modified basis. The most that can be said is that, on a purely hypothetical basis, there might at some point be some incidental, but as yet undefined, effect on interstate commerce but, given the strong legitimate state interests and local benefits sought to be effected by the state action, the possibility that an incidental effect might be felt somewhere by someone does not rise to the level of a prohibited "excessive" burden on interstate commerce, if a burden at all. *Peerless, supra; Pike v. Bruce Church, Inc.,* 79 U.S. 137, 142 (1970); *Arkansas Electric Cooperative Corp. v. Arkansas Public Service Commission,* 461 U.S. 375 (1983); *Pacific Gas &*

Electric Co. v. State Energy Resources Conservation & Development Commission, — U.S. —, 103 S.Ct. 1713 (1983).

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STATEMENT OF THE CASE

The facts giving rise to this case are largely, if not wholly, undisputed and are set forth in the opinion below. 457 So.2d at 1307-1312.

Our discussion relevant to the question of whether this Court should note probable jurisdiction most appropriately begins with a review of the state interests sought to be effected, the simple conditions which the state has placed on Transco's takes of gas, and, almost as important, what the state has not required of Transco.

The State Interests Sought to be Effected, and the Conditions Placed on Transco's Takes of Gas

The state ratable take requirement at issue is intended to prevent reasonably avoidable drainage between gas units, to afford each "owner" in a pool the opportunity to recover his just and equitable share of gas from a pool, and to make that opportunity meaningful by giving each owner access to the market which is available at the wellhead. The requirement also protects a given owner in a pool from discriminatory and irrational treatment by a gas purchaser simply because of who the owner *is not*, or the relatively small size of the owner's interest, or the owner's lack of business sophistication and economic bargaining power. Given that the owners in a pool are possessed of "co-equal and correlative rights" and that "gas is gas", there is no reasonable or rational basis for a gas purchaser who takes gas from a pool refusing to deal with some of the owners in the pool, or offering to

buy an owner's gas, but on terms which are substantially different from those extended to other owners in the same pool.

Under Mississippi law, each owner in a pool of oil and gas is possessed of "co-equal and correlative rights" in a pool of oil and gas so that each owner "may obtain his just and equitable share of production therefrom." Miss. Code Ann. § 53-1-1 (1972). To this end, the Board is empowered to protect against "waste" which is defined to include:

> "Abuse of the correlative rights and opportunities of each owner of oil or gas in a pool due to non-uniform, disproportionate, or unratable withdrawals causing undue drainage between tracts of land or resulting in one or more owners in such pool producing more than his just and equitable share of the production from such pool."

Miss. Code Ann. § 53-1-3(k)(3) (1972). These principles, of course, are not unique to Mississippi; they are uniform to all of the oil and gas producing states.

The state's ratable take requirement at issue implements these principles, is two-fold and is very simple: First, if and when a gas purchaser takes federally-deregulated gas from a pool, the purchaser must offer to take whatever quantities of gas the purchaser desires ratably from all of the wells in order to allow each owner in the pool the opportunity to recover his just and equitable share of oil and gas, to prevent some owners from recovering more than their just and equitable share, and to prevent drainage and reservoir damage, caused by unratable and disproportionate takes of gas from the wells which produce from a pool. Second, for the gas of those owners who do not have a contract with the purchaser, but who want to sell their federally-deregulated gas, the

purchaser must offer to pay a "reasonable price, determined by reference to prevailing market conditions and other appropriate economic considerations," 457 So.2d at 1331, in order to make meaningful those owners' right to recover their just and equitable share of production from the pool.

Without the benefit of this state protection, an owner in a pool, particularly an owner of a small interest, can easily find himself denied the opportunity to recover his just and equitable share of gas in the pool because of, *inter alia,* an operator or co-owners who attempt to allocate all production to themselves, or a purchaser who refuses to buy the owner's gas. That is precisely the quandry in which Coastal found itself in the Summer of 1982. That is precisely what led to the state ratable take order in question.

What the State Has Not Required

Given the many misrepresentations that have been made about what the state supposedly has required of Transco, it is an appropriate time to consider just what the state has *not* required.

The state has not required Transco to take more gas than it needs, nor to take the full allowable of any well(s), nor to take the full allowable of any pool, nor to give any producer a contract, nor to pay anyone "take-or-pay money," nor to pay a fixed price, nor to pay a higher-than-market price--nor to take any gas at all. Thus, Transco's representations that Mississippi has required production "in excess of market demand" has no basis in fact. It is a misrepresentation, pure and simple.

The six-well pool in question has an "allowable" which, under state law, is the maximum amount of gas

which may be taken from the pool. The allowable is based on the "maximum efficient rate of production" by all of the wells which produce from the pool. Thus, the allowable for the pool is *the ceiling,* not the floor, on production and takes of gas. In any given month or period of time, Transco, judging what its needs are, may take 100% of the pool's allowable, or 1% of the pool's allowable, or no gas at all. The conditions Mississippi has placed on Transco's takes of deregulated gas do not require Transco to take more expensive gas to the exclusion of cheaper gas, nor to favor Mississippi gas over other states' gas, nor to pay the non-contract owners the "highest price" paid in the field. The state's requirement is simple: When and if Transco decides to take the federally-deregulated gas from the pool in question, Transco must offer to take the gas it needs ratably from the wells which produce from the pool and, unless Transco and an owner agree otherwise, Transco must offer to pay an owner with whom it has no purchase contract a "reasonable price, determined by reference to prevailing market conditions and other appropriate economic considerations." 457 So.2d at 1331. The state has not even attempted to dictate what that price should be. Transco has responded to this requirement by paying the non-contract owners a "market-out" price.

These are the *only* conditions which the State of Mississippi has placed on Transco's takes of gas from the deregulated gas pool in question. The conditions are simple and easily complied with. Witness the undisputed fact that, since December 1982, Transco has been taking gas ratably from the pool and paying a "market-out" price for the gas of the non-contract owners.

ARGUMENT

I.

THE PRESUMPTION QUESTION IS NOT SUBSTANTIAL

The preemption question in this case[1] is not substantial because the plain, unequivocal language of Section 601 (a)(1)(A)&(B) of the NGPA and the accompanying Conference Report of Congress so clearly state that the first sale and purchase of the federally-deregulated natural gas in question[2] no longer is subject to either the NGA or FERC's jurisdiction under the NGA. Thus, as to the federally-deregulated gas at issue, Section 601(a) (1) has eliminated what has always been the *only* statutory reason for invalidating a state ratable take requirement.

How did we come to this point? By two roads. First, down a road of NGA/FERC regulation of the first sale transaction between a producer and an interstate gas purchaser, a comprehensive regulation which ultimately led to artificially low NGA-mandated "just and reasonable" wellhead prices, low prices which led to a lack of incentive for producers to drill for new gas and sell that gas into

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[1]The preemption question as framed by Transco is not merely inaccurate and imprecise—it is ridiculously overstated, presumably for "shock effect." The question has never been framed that way in the proceedings to date. To the contrary, the preemption question has always been, what is now the relevance and application of *Northern Natural* to NGPA—deregulated natural gas in light of NGPA Section 601(a) (1)? *Transco, supra,* 457 So.2d at 1315.

[2]The gas in question is both deregulated gas (meaning that it has been classified as "deep, high-cost gas" under NGPA Section 107(c) (1), and undedicated gas (meaning that it was not committed or dedicated to interstate commerce as the day before the date of enactment of the NGPA). See NGPA Section 601(a) (1).

interstate commerce, a lack of incentive which ultimately led to the severe interstate gas shortages of the mid-1970s, shortages which have been described as a "national crisis." That is the same road which led to the *Phillips* decision in 1954 and to *Northern Natural* in 1963.

The nation's recovery from that abysmal situation began in 1978 when Congress turned down a second road, a road of NGPA regulation-to-deregulate which eliminated the difference between the interstate and intrastate markets, and provided producers and interstate gas purchasers alike with the degree of freedom from federal regulation and with the price incentives which Congress determined were needed in order to allow the price of gas *to rise* and encourage producers to discover and produce new gas and sell that gas into the interstate market. NGPA Section 601(a)(1) was the vehicle used to eliminate federal regulation of the first sale and purchase of certain types of natural gas, including the deregulated natural gas at issue. It is the elimination of that federal regulation which has freed the state, once again, to apply a simple ratable take requirement to the first sale and purchase of federally-deregulated gas. The state's authority to make that kind of requirement was recognized by this Court thirty-five (35) years ago in *Peerless*.

Peerless

The producer in *Peerless* found itself in virtually the same quandry as did Coastal: The interstate gas purchaser who was buying from the pool first refused to buy Peerless' gas at all, and then offered to buy the gas at a price which was lower than that being paid to other own-

ers in the field. The state conservation commission then entered a ratable take order requiring the purchaser to take gas ratably from the pool and to pay Peerless a fixed minimum price. This Court, in a unanimous decision, rejected challenges to the order made on the grounds of the Due Process, Equal Protection and Commerce Clauses.[3]

In *Peerless,* however, the Court made the cryptic observation that it was not considering the effect the NGA might have on a state ratable take order. That effect was considered thirteen years later in *Northern Natural,* which was decided after the 1954 decision in *Phillips.*

Phillips

At the time *Peerless* was decided, the NGA had not been construed to apply to the first sale transaction between a producer and an interstate gas purchaser. Four (4) years later, however, the Court's decision in *Phillips* extended the NGA, and the FPC's jurisdiction thereunder, to cover a producer's sale of gas to an interstate pipeline, thus allowing the FPC to determine whether the gas could be sold into interstate commerce and whether the sales price was "just and reasonable." Distinguishing *Peerless,* the Court reiterated the aim of the NGA:

> "Protection of consumers against exploitation at the hands of natural-gas companies was the primary aim of the Natural Gas Act. * * *"

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[3]In a companion case to *Peerless, Phillips Petroleum Co. v. Oklahoma,* 340 U.S. 190 (1950) the Court upheld a similar minimum price order issued by the Oklahoma Corporation Commission.

347 U.S. at 685. *Phillips* launched a twenty-five (25) year period during which the FPC (later FERC), under Section 1(b) of the NGA, controlled all facets of a producer's sale and an interstate pipeline's purchase of gas. The "red tape" was so burdensome and the "just and reasonable" prices set by the FPC were so artificially low that, as the years passed by, the prices provided little or no incentive for producers to develop new gas reserves and sell that gas into the interstate market. The "pay-off" for the "protection of consumers" philosophy turned out to be a severe shortage of gas on the *federally*-regulated interstate market, while there developed a corresponding surplus of gas on the *state*-regulated intrastate market.

Northern Natural

Northern Natural was an extension of *Phillips*. The Court, in a less-than-unanimous decision, held invalid a ratable take order which the Kansas Corporation Commission entered against an interstate pipeline company because the state order invaded what was *then* the FPC's exclusive regulatory jurisdiction under Section 1(b) of the Natural Gas Act of 1938 (NGA):

> "We disagree with the Kansas Supreme Court, for we hold that the State Commission's orders did invade the exclusive jurisdiction which the Natural Gas Act has conferred upon the Federal Power Commission over the sale and transportation of natural gas in interstate commerce for resale."

372 U.S. at 89. The limited statutory basis for the result in *Northern Natural* is evidenced by the fact that the Court was careful to point out that it was not overruling

Peerless.[4] Thus, the state order was not invalidated because of some vague concern about the "imminent possibility of conflict" with federal law; it was invalidated on a narrow statutory ground because of a direct and ascertainable conflict with the FPC's *then existing* exclusive jurisdiction[5] under Section 1(b) of the NGA to grant or

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[4]372 U.S. at 91, note 10. *Peerless* was most recently cited in a NGPA context in *Energy Reserves Group, Inc. v. Kansas Power and Light Co.*, — U.S. —, 103 S.Ct. 697 (1983). There, the Court cited *Peerless* for its holding that a state has the power to regulate natural gas prices and sales so long as that regulation does not interfere with the Commerce Clause:

> "State authority to regulate natural gas prices is well established. *See Cities Service Gas Co. v. Peerless Oil & Gas Co.* * * *
>
> "On several occasions, the Court has approved state price regulation of natural gas that did not interfere with interstate commerce. See, e.g., . . . *Cities Service Gas Co. v. Peerless Oil & Gas Co.* * * *"

— U.S. at —; 103 S.Ct. at 706, notes 16 & 17.

[5]The Court in *Northern Natural* stated that with respect to the NGA "[t]he Congress enacted a comprehensive scheme of federal regulation of *'all wholesales* of natural gas in interstate commerce, whether by a pipeline company or not and whether occurring before, during, or after transmission by an interstate pipeline company.' " 372 U.S. at 91. [Emphasis added]. Compare *that* pre-NGPA view of the Court with the Court's post-NGPA view of the state of the scheme of federal regulation, in *Public Service Commission v. Mid-Louisiana Gas Co.*, — U.S. —, 103 S.Ct. 3024 (1983):

> "The NGPA is designed to preserve the Commission's authority under the NGA to regulate natural gas sales from pipelines to their customers; *however, it is designed to supplant the Commission's authority to establish rates for the wholesale market, the market consisting of so-called 'first-sales' of natural gas.*" — U.S. at —, 103 S.Ct. at 3031. [Emphasis added].

deny the entry of gas into the interstate market, and to fix the "just and reasonable" wellhead sales price of that gas. It was precisely that jurisdiction which was eliminated by NGPA Section 601(a)(1).

The NGPA

In enacting the NGPA, Congress had two central goals: First, to provide price incentives to producers to drill more gas wells, find new gas and put that new gas into the interstate market. Second, to free producers and pipelines from those regulatory features of the NGA and FERC's jurisdiction which were discouraging producers from selling gas to the pipelines and were crippling pipelines' ability to purchase new gas.[6]

Those congressional goals were reached by Congress, first, eliminating FERC's NGA-jurisdiction and powers to require a producer and a pipeline to obtain FERC's approval of the entry of new gas into the interstate market and the price to be paid by the pipeline for that gas, and, second, enacting immediate price deregulation for some new gas (like "deep, high-cost gas" under Section 107), and gradual price deregulation for other new gas (like gas under Sections 102 and 103). Sections 121 and 601 of the NGPA accomplished these goals.

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[6]See, e.g., *Pennzoil Co. v. FERC*, 645 F.2d at 378: "The NGPA is a fundamental change in regulatory outlook. * * * FERC has a fundamentally different regulatory obligation. . . . The balance Congress struck already took into account the conflicting interests of producers and consumers." In *Pennzoil*, the Court concluded that the effect of § 601(a)(1)(A) was to deny FERC the authority to regulate or interpret gas purchase contracts covering "undedicated" gas. *Id.* at 380. *See also Mid-Louisiana Gas Co. v. FERC*, 664 F.2d at 530, 535 (5th Cir. 1981).

Section 121 provided producers with the price incentives needed to encourage them to find new gas and sell that gas into the interstate market. Thus, Section 121 immediately eliminated price controls for Section 107 "deep, high-cost gas" and set a 1985 date for price deregulation of other new gas, such as gas qualifying for pricing under Sections 102 and 103. Section 121 thus furnished *the price incentives* which Congress intended.

Section 601 provided producers and pipelines with the freedom from regulatory interference by FERC with a pipeline's purchase and a producer's sale of new gas in order to enable a pipeline to freely compete for new gas by allowing the pipeline to pay a producer the higher incentive prices or deregulated prices for new gas (without *ever* having to get FERC approval of the prices paid or the other terms of the contract) and to exempt a pipeline and a producer alike from the then existing regulatory constraints of the NGA and FERC's jurisdiction under the NGA, constraints which had combined with low FERC-set "just and reasonable" prices to produce the severe gas shortages of the late 1970s caused by the producers' reluctance (and sometimes refusal) to sell their gas to interstate commerce, and the pipelines' inability to buy new gas from the producers. Section 601 thus furnished the pipelines and the producers with *the degree of freedom from regulatory interference* by FERC which Congress intended.[7]

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[7]*See*, e.g., *Tenneco, Inc. v. Sutton*, 530 F.Supp. 411, 419 (M.D. 1981): "These provisions [Section 601] remove the Commission's authority to establish just and reasonable

(Continued on next page)

Section 601 of the NGPA

Section 601(a)(1) eliminates FERC's NGA-jurisdiction to control, or regulate, either directly or indirectly, a producer's sale and a pipeline's purchase of deregulated gas.[8] Thus, Section 601(a)(1) eliminates the NGA re-

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prices under the NGA for producer sales into the interstate market and to indirectly regulate these sales through control of the interstate pipeline purchaser's pass-through of purchase gas costs."

See also the "Curtis/Jackson Letter", Federal Programs Advisory Service (FPAS) § 601:220 (9-8-78), on Section 601: "This section [601] executes the legislative intent to remove from Natural Gas Act utility type regulation natural gas not heretofore dedicated or committed to interstate commerce (§ 601(a) (1) (A), and to remove from Natural Gas Act-type regulation heretofore jurisdictional sales of high cost gas, gas from new OCS leases, new well qualifying for the new natural gas price under section 102, and [103 gas] (§ 601 (a) (1) (B)." FPAS § 601:220, page 2.

[8]The "Joint Explanatory Statement of the Committee on Conference" of the Congress, which accompanied the NGPA, is extremely important because it states in plain English what Section 601(a)(1) means:

> "The Conference Agreement limits the jurisdiction of the Commission under the Natural Gas Act in a manner similar to the House-passed bill.
>
> Natural gas not committed or dedicated to interstate commerce as of the day before the date of the enactment of this Act is *never* made subject to the Commission's jurisdiction under sec. 1(b) of the Natural Gas Act. The Commission's jurisdiction under section 1(b) of the Natural Gas Act *ceases* on the first day of the first month beginning after the date of enactment of this Act for the following categories of natural gas:
>
> High-cost natural gas which qualifies for deregulated price treatment under section 107(c) (1), (2), (3), or (4); * * *" [Emphasis added].

See, e.g., Pennzoil Co. v. FERC, supra, 645 F.2d at 378.

quirement that the parties must first obtain from FERC a certificate of public convenience and necessity as to new gas, and removes FERC's jurisdiction and power to set a "just and reasonable" price and dictate contract terms. The *effect* of this particular sub-section is that neither the producer nor the pipeline ever has to obtain the previously required certificate of public convenience and necessity in order to sell and buy this type of new gas.[9] Because the parties do not have to obtain a certificate from FERC, FERC cannot use its NGA power (to grant or deny a certificate) to control purchases, contract terms and price, as it did prior to enactment of the NGPA.[10] Nor can FERC, pursuant to its NGA jurisdiction over a "natural gas company," control the price which a pipeline, like Transco, pays for the gas on the grounds that

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[9]*See*, e.g., *Conoco, Inc. v. FERC*, 662 F.2d 796, 797, 799 (5th Cir. 1980). *See also* FERC's Preamble to the issuance of the first interim regulations issued after the NGPA was passed, 43 F.R. 56448 (12-1-78), wherein FERC observed the effect of the NGPA on the NGA:

> "If gas is not committed or dedicated to interstate commerce . . . or is exempted from the jurisdiction of the NGA under section 601(a) (1) (B) as [107 or 102 or 103 gas] the prior framework of utility-type regulation under the NGA no longer applies.
>
> If natural gas sales are freed from the requirements of the NGA, several adjustments to NGA regulations are obviated. First, there is no longer any necessity for a producer to seek certification of the sales as serving the public convenience and necessity."

[10]*See*, e.g., *Pennzoil Co. v. FERC, supra*, in which the court held that FERC no longer has jurisdiction to regulate or interpret gas purchase contracts covering undedicated gas or dedicated gas which is also 107 or 102 or 103 gas: "In other words, section 601(a) (1) (A) prevents the universe of gas subject to the NGA from expanding." 645 F.2d at 380.

Transco is an otherwise regulated "natural gas company." Section 601(a)(1)(D) takes care of that potential problem by providing that neither party to the first sale transaction of deregulated gas shall be considered to be a "natural gas company" with respect to its purchase of deregulated gas.

Section 601(b) and (c) protect a pipeline from an after-the-purchase attack by FERC on the price paid by the pipeline for deregulated gas. Section 601(b) provides that all prices which a pipeline pays for deregulated gas are deemed "just and reasonable" as a matter of law, and Section 601(c) provides that the pipeline has the guaranteed statutory right to pass-through the price which it pays for deregulated gas and include that price in its resale rates charged to consumers, unless the price is the result of "fraud, abuse or similar grounds."[11]

There Is No Arguable Conflict Between Mississippi's Ratable Take Requirement and the NGA/NGPA

Obviously, the NGPA regulatory scheme is vastly different from the NGA regulatory scheme which prevailed when *Northern Natural* was decided. There *now* is neither an actual nor a hypothetical conflict between the state ratable take requirement at issue and, on the other hand, the NGA and the NGPA.

To review, at the time *Northern Natural* was decided, the FPC (now FEPC) had two fundamental regulatory powers over gas which was destined for an interstate

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[11]*See, e.g., Pennzoil Co. v. FERC, supra,* 645 F.2d at 379, n.38: "Section 601(c) (2) guarantees to interstate pipelines the ability to pass through NGPA payments."

market. First, before the gas could even enter the interstate market, the producer and pipeline had to obtain a certificate of public convenience and necessity from the FPC; they were not free to simply put the gas into the interstate market without FPC approval. Second, the price paid by the pipeline had to be first approved by the FPC as a "just and reasonable price"; the producer and pipeline were not free to simply negotiate a price. There were no ceiling prices as such, only "just and reasonable" prices, and there was no interstate gas which was not subject to federal price regulation.

That was the federal regulatory scheme with which the Kansas ratable take/minimum price order collided in *Northern Natural.* The order interferred with both of what were *then* the FPC's fundamental regulatory powers because the order forced gas into interstate commerce, without a *then* required certificate of public convenience and necessity, and set a minimum price to be paid for the gas, without a *then* required prior adjudication by the FPC that the minimum price was "just and reasonable".

What changed with enactment of the NGPA? First, a certificate of public convenience and necessity is no longer required before undedicated or deregulated gas can enter the interstate market; the producer and pipeline are free to put the gas into the interstate market at anytime. This, of course, is consistent with the overall goal of the NGPA—to get *more* gas into interstate commerce with less red tape. Second, FERC has no jurisdiction over and no authority to set the "first sale" price to be paid by the pipeline for deregulated gas; under Section 601(b)(1)(A) the price paid by the pipeline for deregulated gas is presumed to be "just and reasonable" and no FERC

approval is required before the pipeline can pay that price. Nor can FERC seek to influence or affect the first sale price paid by the pipeline through FERC's jurisdiction over the pipeline's resale rates; under Section 601(c), the pipeline has a guaranteed statutory pass-through of the price it pays for the gas, unless the price results from "fraud, abuse or similar grounds".

The state action at issue stops short of affecting any transaction which continues to be subject to the NGA or FERC's jurisdiction thereunder. The ratable take requirement affects only the wellhead "first sale" price and the initial entry of deregulated gas into the interstate market—it goes no further. It is a case of coincidental state and federal regulation. Where one stops the other starts, and neither infringes upon the other. *Peerless.*

The preemption question, therefore, is not substantial because it is so clear that the NGA and FERC's jurisdiction thereunder do not apply to the first sale of federally-deregulated natural gas, leaving the state free, once again, to attach the ratable take requirement at issue to an interstate pipeline's takes of federally-deregulated gas. *Accord, Peerless, supra.*

II.

THE COMMERCE CLAUSE QUESTION IS NOT SUBSTANTIAL

The Commerce Clause question in this case is not substantial because this Court has held that a state ratable take/minimum price order directed to an interstate gas purchaser does not violate the Commerce Clause. *Peerless, supra.* As we have pointed out, even *Northern*

Natural was careful to point out that *Peerless* remained good law on the constitutional challenges to the state order. 372 U.S. at 91, n. 10.

> "Where the statute regulates even-handedly to effectuate a legitimate local public interest, and its effects on interstate commerce are only incidental, it will be upheld unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits."

Pike v. Bruce Church, Inc., supra, 397 U.S. at 142. Applying that "new balancing test," the Court has accorded the states a wider berth and, consequently, has recently upheld a variety of state regulatory actions which have been carried out against a background of federal regulation. *See, Arkansas Electric Cooperative Corp. v. Arkansas Public Service Commission, supra; Pacific Gas and Electric Co. v. State Energy Resources Conservation and Development Commission, supra; Exxon Corp. v. Governor of Maryland,* 437 U.S. 117, 127-29 (1978); *Minnesota v. Cloverleaf Creamery Co.,* 499 U.S. 456 (1981); *Commonwealth Edison Co. v. Montana,* 453 U.S. 609 (1981). No longer is the Court content to void state action because of the mere possibility that the state action might burden interstate commerce. An actual burden must be shown, and then the interests of the state are to be balanced against the actual burden on interstate commerce to determine if, in light of the "putative local benefits", the burden on interstate commerce is excessive.

Just what is the alleged excessive burden on interstate commerce in this case? The best evidence of the fickle nature of the alleged burden is Transco's own framing of the Commerce Clause question:

> "Does Mississippi's attempted regulation of interstate pipeline companys' purchase of 'high-cost' gas constitute an impermissible burden on interstate commerce *under present market conditions?*" [Emphaphis added].

This, of course, is a "weather vane approach" to the Commerce Clause: If the forecast is that compliance with the state requirement may cause Transco any kind of economic burden, then the state's requirement rises to the level of an excessive burden on interstate commerce. Individualized and seasonal burdens, however, are not what the Commerce Clause proscribes.

Factually, the alleged burden in this case is not some imagined "complex task" of balancing well production; there is no such complex task. The burden Transco complains of has its beginning and its end in a few of Transco's gas purchase contracts. Transco has entered into some relatively few gas purchase contracts under which Transco has agreed to pay some few producers two or three times the market price for their gas. Transco's gamble in entering into those contracts was that Transco could mix its expensive gas with its cheap gas and still have a marketable, price competitive and *profitable* product — one which would allow Transco to realize its maximum allowed rate of return. Transco also agreed to pay those few producers what Transco now considers to be "excessive" minimum annual payments, so-called "take-or-pay payments." Because of the reduced demand for gas in general, Transco claims that, if it offers to take gas from the non-contract owners in the six-well pool in question, then Transco's take-or-pay obligations to its contract owners in the pool *may* increase. Thus, behind Transco's representations that Mississippi has "forced" Transco to take "high-cost" gas are the facts that (1)

from time-to-time Transco has tied its ratable takes of gas from the pool to its minimum annual take obligations provided for in its contracts, in order to hold down its take-or-pay payments to its contract owners; (2) Transco is not incurring and *will never incur* any take-or-pay obligations to the non-contract owners; and (3) since December 1982, Transco has been paying the non-contract owners only a "market price" for their gas.

Thus, Transco's fickle characterization of the Commerce Clause "question" in this case is directly attributable to the fact that, but for the temporary reduced demand for gas and those relatively few of Transco gas purchase contracts in which Transco agreed to pay two or three times the market price for deep gas and to make "excessive" take-or-pay payments, all without the protection of a "market-out clause" which would allow Transco unilaterally to reduce those contract prices, it would be "convenient" for Transco to comply with the state ratable take requirement at issue. To paraphrase, there would be no burden on interstate commerce if Transco's "present market conditions" were "better."

Obviously, the "burden" in question is not a burden on interstate commerce in general, much less an excessive burden. The burden, if any, is *Transco's* burden which has been caused by some of *Transco's* contractual practices. Other pipelines, who were more conservative or prudent in their offers, do not have these "burdens." Thus, to indulge Transco's claim is to have the Commerce Clause question turn on the happenstance and vagaries of the marketplace or the economic miscalculations of one party or the other. It is to make the Com-

merce Clause a safe-harbor for one who has rolled the dice and lost.

The ultimate irony, of course, is that the state has not required Transco to take any set quantities of gas (as do Transco's contracts), nor has the state required Transco to pay more than a market price for any gas (as do some of Transco's contracts), nor has the state required Transco to make any take-or-pay payments (as do Transco's contracts). The state has required *only* that, if and when Transco takes federally-deregulated gas from the pool in question, Transco must offer to take that gas ratably from the wells which produce from the pool and must offer to pay the non-contract owners in the pool a market price—the very price which Transco ends each working day wishing that it could pay to all of its contract owners.

In conclusion, the simple ratable take requirement at issue is not a burden on interstate commerce "under present market conditions" or otherwise. The ridiculous misrepresentations of what the state allegedly has required of Transco have been made to divert attention from the undisputed fact that the *only* conceivable burden on anyone from complying with the state requirement at issue is the short-term "burden" that Transco *might* incur some contractual take-or-pay obligations to some of its contract owners. That contingency, if and when it ever matures and Transco actually makes the take-or-pay payments, might put Transco out of the time value of some refundable take-or-pay monies, but it does not constitute a burden on interstate commerce, much less rise to the level of a prohibited excessive burden on interstate commerce. Simply put, Transco's Commerce Clause claim is frivolous. *Peerless, supra.*

CONCLUSION

This case should be dismissed, or alternatively, the decision of the Mississippi Supreme Court should be affirmed for lack of a substantial federal question.

Respectfully submitted,

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